

## **Penney has 1Q loss as new pricing repels shoppers**

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Turns out, J.C. Penney shoppers don't prefer predictable pricing over blockbuster bargains — at least not yet.

The department-store chain on Tuesday reported a larger-than-expected first-quarter loss largely because customers were turned off by the retailer's new plan to get rid of big sales throughout the year in favor of everyday low pricing.

The idea of the strategy, which was rolled out on Feb. 1, is to discourage shoppers from waiting for the nearly 600 sales Penney used to offer each year. But the move has backfired: It seems many faithful Penney customers have stopped shopping altogether.

Wendy Ruud, 49, used to visit the Penney store near her home in Boca Raton, Fla. every two weeks. But Ruud hasn't been back to the store since early this year when she stopped getting coupons from the retailer in her email inbox.

"The closest J.C. Penney is about a half hour away from me," said Ruud, who has been shopping more at Target and Wal-Mart. "If I don't get a special discount, it's not worth the trip."

The lackluster reception to Penney's new pricing strategy underscores how difficult it is for a company to change the way consumers behave. Industry watchers say Penney faces an uphill battle in attempting to shift the mindset of its shoppers, who increasingly have become accustomed to and spoiled by fat discounts during the economic downturn.

"Consumers want deals, and they're willing to wait for them," said C. Britt Beemer, chairman of America's Research Group, a consumer research firm. "When you train customers to shop at big discounts, that customer is not going to change."

The first hint that Penney's new pricing plan wasn't resonating with customers came last week when Macy's CFO Karen Hoguet told analysts that sales were rising at Macy's locations that share the same mall as Penney stores.

J.C. Penney Co.'s first-quarter results just affirm that customers have been slow to warm to its pricing plan. The company, based in Plano, Texas, lost \$163 million, or 75 cents a share, in the three months ended April 28, compared with a profit of \$64 million, or 28 cents a share, in the year-ago period.

Revenue dropped 20 percent to \$3.15 billion for the quarter as customer traffic slipped 10 percent. Meanwhile, revenue at stores opened at least a year — a figure

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used to measure a retailer's health — was down 18.9 percent. That's a much steeper fall than the 11.4 percent drop Wall Street was expecting.

Ron Johnson, a former Apple Inc. executive who became Penney's CEO in November, acknowledged that the first quarter was "tougher than anticipated." At a meeting with analysts and investors on Tuesday, Johnson said that he expects 2012 to be a difficult year.

"We had to make the bold step," in pricing, he said. "It's one big year we have to go through. It's really hard but we'll get through it."

Penney has said that it will take time for the pricing plan to work. But the first-quarter results put pressure on Johnson to deliver results at Penney, which has been hurt by the economic downturn as its core middle-income shoppers have cut back on spending.

Johnson has said he wants to transform every aspect of the department-store chain, from the brands it carries to the way it displays them in stores. Investors had put a lot of faith in Johnson, who was behind both Apple's successful retail stores and Target's move toward cheap chic before that. But they've increasingly soured on his pricing plan.

Penney shares soared 24 percent to about \$43 after Johnson announced the strategy in late January. But since the middle of February — after the new pricing was rolled out in stores— investors have sent shares back down to around \$34. After Penney reported the disappointing first-quarter results after the markets closed on Tuesday, its shares fell 12 percent to \$29.30 in after-hours trading.

Investors aren't the only ones watching Penney's plan closely. If the everyday pricing strategy does well, other chains could follow. Indeed, many clothing chains are desperate to wean shoppers off the big discounts that have become commonplace since the Great Recession began in late 2007.

"This is an ambitious task," said Chris Donnelly, managing director of Accenture's retail practice. "If Penney succeeds, (stores) will have to decide whether they'll follow."

In order for Penney's pricing plan to succeed, analysts say the retailer will need to do a better job communicating it to customers. Penney's plan is more complex than Wal-Mart's iconic everyday low pricing strategy: It doesn't aim to undercut competitors, but rather focuses on offering customers predictable prices.

The company has run ads to explain to shoppers its three-tiered pricing strategy, which features everyday prices that are about 40 percent less than a year ago, monthlong sales on select items and clearance events during the first and third Friday of each month.

But some observers say Penney's ads — which mimic rival Target's whimsical style — are confusing. In one TV spot, for instance, a dog donning a birthday hat

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continuously jumps through a hula hoop that a young girl is holding. The text reads: "No more jumping through hoops. No coupon clipping. No door busting. Just great prices from the start."

"I think they're trying to be too cute and entertaining," said Laura Ries, president of Atlanta-based brand strategy firm Ries and Ries, which has worked with Walt Disney and Microsoft. "I think a more direct message would work better."

Penney said on Tuesday that it plans to tweak its ads to better spell out the new plan, including how much lower the everyday prices are from last year. The retailer also said that starting in the fall 47 percent of its merchandise will be new — the result of it dumping some brands while redesigning others.

It also announced a slew of new popular designers including Vivienne Tam and Betsey Johnson who will be selling affordable versions to Penney. Additionally, the company plans to launch a new brand under the "JCP" label this fall.

Those changes are in addition to ones Penney previously announced. The chain plans to add about 100 shops within each of its stores by 2015 that will either focus on one brand or a variety of labels. The company also is planning to add areas in its stores called Town Squares to offer services and advice.

Analysts say that Penney will have an easier time conveying the everyday pricing plan once shoppers start to see new brands and other changes that the retailer is making in the stores.

"I am rooting for Ron Johnson to hit a home run," said Ronald Friedman, the head of the retail group at Marcus LLP, an accounting firm that works with clothing companies. "But it won't happen overnight. This is a process. It will take between 12 to 18 months."

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